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Modernizing Michigan's Tax Structure: Some things old, Some things new...

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Introduction & Disclaimers

- Legislative staff
- Executive Branch roles
- Academic
 - Michigan State
 - Western Michigan
 - Wayne State University, State Policy Center 1998
- Retiree member and Chair, State Employees Retirement Board
- Public Policy Associates, Group Manager and Senior Policy Consultant 2005
- Views expressed are my own



About these suggestions

- In some cases I specifically suggest use of an item for increased revenue
- In others, I specifically suggest revenue neutrality
- These are suggestions only
- You and your colleagues, and the people of Michigan are the final arbiters of the balance of enhancements, cuts or revenue neutrality
- I submit only that given the size of the structural challenge you face, you will need more revenue

First , about the new...

- Repeal the MBT
- Do a revenue neutral replacement via a graduated income tax
- Because the graduated income tax requires voter approval, structure this as a tie-barred change—that is, if the ballot proposal doesn't pass, the MBT remains in place

Why repeal the MBT?

- It seems to be uniformly not understood, and widely reviled in the business community—even though lots of businesses had to have been winners...why haven't they come forward?
- Michigan is wasting way too much time on what I believe is the wrong issue—we need to be talking about future goals—and the path to reach them
- Not having a general business tax should be the ultimate tax incentive! And it may allow additional reforms to end some of our collection of other “odds and ends” tax incentives

What Kind of Graduated Income Tax?

- Seek simplicity: consider no more than about 5 income brackets if you choose to go with a state based approach
- Seek simplicity: consider the option of calculating the state tax due as a percentage of the federal tax due
 - Example: Rhode Island's state income tax is calculated as 25 % of the federal liability of its residents

Pros and cons?

- Pro-Michigan desperately needs to put aside decades of non-productive arguing about business taxes
- Pro-to help eliminate the perennial structural deficits, Michigan needs more growth potential in its revenue structure
- Con-historic resistance to graduated tax
- Con-more growth potential also means more volatility

Second, expand Sales & Use Tax Base to include selected services

- Admissions and amusements, sports (professional & perhaps college, MIS), theaters, movies, museums (Greenfield Village), bowling and golf!
 - People still go to Disney World even though Florida taxes the tickets!
- Services that are primarily to individuals, not businesses
 - Beauty and barbershops; laundry and dry cleaning; cleaning of homes, landscape and lawn services, repair services; legal services to individuals
- Use these for increased revenue part of budget solution

Third, modernize the structure of some old taxes

- Convert beer, wine, tobacco from unit base to ad valorem
- Make these changes revenue neutral at the start, and allow them to grow over time

Fourth, annually review tax exemptions for policy effectiveness

- Set staggered sunset dates on all to force evaluation
- Set measurable criteria to evaluate effectiveness of all that are renewed
- Set a goal of “X \$\$” to come from the first reviews as part of budget solution
- Start with the largest 20 by dollar size as estimated in the Tax Expenditure report
- Remember, with no general business tax you may not need other business incentive exemptions

Fifth, restore some old taxes...

■ Intangibles Tax

- Intangibles tax was one of most progressive taxes in Michigan system
- Needed a lot of investment income to pay it

■ Inheritance/Estate Tax

- Federal tax will continue in some form after 2010
- A state credit is a virtual certainty
- Why not keep Michigan dollars in Michigan?

Sixth, work to restore funding to Budget Stabilization Fund

- If and when recovery comes, resist pressure to spend funds as they come in
- Michigan is likely to remain a volatile economy for many decades
- The sun will come out tomorrow, but we'll also have more rainy days and we should be smart enough to not be surprised by them

Seventh, evaluate the expenditure side of the budget as well

- Public services by definition should be available to all who qualify
- Some **methods** of service delivery may be more effective than others for same amount of services
- **Build in performance criteria** to give future legislators an objective way to measure that effectiveness: for new programs and any new tax incentives

Eighth, structural reforms take time

- One of the House Speakers I had the privilege to work for used to remind us that
 - “For every complex problem there is always a simple, easy solution.”
- **“Unfortunately,” he also said, “that simple solution is almost always wrong, and at best incomplete.”**

Conclusion

- Resolving the depth of the structural deficit will take time, courage, and compromise
- Everyone will need to step back from some strongly held values to forge those compromises
- Failure to do so almost certainly means that you and Michigan will endure a really painful replay of a tragic, not a comic, version of Bill Murray's "Groundhog Day"



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